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ABSTRACT

A competent staff in financial administration at an institution of higher education is not adequate in itself. The volume of transactions is too great, the external restraints too numerous, and the stakes too high to deny the value of an independent audit. It is in the best interests of the institution to develop a receptive attitude toward auditors and to assist in facilitating the conduct of the audit. Steps that both the institutional staff and the auditors can take to contribute toward improved mutual relationships in financial audits are presented. (MJM)

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A Look at Audit Relationships

ON LIVING WITH AUDITORS

By Max A. Binkley

Certain changes in higher education administration during the last several years have prompted colleges and universities to improve their standards for accountability and fiscal control. Among these are the increasing use of certified public accountants for audits, steps taken by professional organizations toward statements of accounting standards, and in particular the reliance on federal funds subject to the examinations of federal auditors. Public institutions have additional inducement to meet higher standards of financial administration in those states where the professionalism of state controllers and state auditors has been improved.

A comparison between past and present audit reports of public institutions could lead to the false conclusion that there has been serious deterioration in institutional financial reports over the years. However, it is more likely that in earlier years the standards of both the institution and the state auditor were low compared to those of the present. For example, a decade or so ago the state auditor's staff may have devoted fifteen man-weeks to an institutional audit and subsequently released a brief report indicating everything was shipshape. Today, ten to twenty times the manpower may be allotted to the same job, and the auditor's comments may be lengthy and list numerous deficiencies.

Current financial reports of state universities and colleges probably are much more reliable than formerly. The transition has occurred in various degrees in different states. In cases where a rise in the state auditor's standards preceded action by institutions, the institutional staff could only react by trying to upgrade their operations. They suffered the consequences of the inevitable time lag between efforts and results. Other state institutions took the initiative and began programs of self-examination and self-improvement, thereby preserving the confidence of the legislatures and the public.

A financial audit invariably results in findings, since the performance of the institution is never without flaw. But it is the degree to which the findings are consequential that affects confidence in the fiscal operation of the institution.

A competent staff in financial administration is not adequate in itself. The volume of transactions is too great, the external restraints too numerous, and the stakes too high to deny the value of independent audit. It is in the best interests of the institution to develop a receptive attitude toward auditors and to assist in facilitating the conduct of the audit.

The Role of Auditors

It may be difficult to achieve a positive attitude under certain circumstances. Where colleges and universities have failed to improve financial administration to meet the requirements of new and complex programs and responsibilities—particularly where institutions have failed to meet new standards imposed by external authorities—the audit can result in findings of numerous significant deficiencies. In this situation the problems of the institution tend to multiply. The auditors may work for months in their attempt to conduct a conclusive examination. Involvement with the auditors may leave institutional personnel with little or no time to plan and implement the improvements needed.

The difficulties are compounded if two or more sets of auditors are making examinations simultaneously. In at least one case three different sets of auditors were at work at the same time: state auditors, federal auditors, and a CPA firm, each group primarily concerned with different aspects of the operations but inevitably overlapping.

When internal controls and procedures are deficient, the auditors may bring so many problems to light that the staff

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HE 006 164

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of the institution learns of problems much faster than it is able to solve them. It is difficult to work toward improved relationships with the auditors at such a time. However, auditors' findings and reports and their discernment of deficiencies may give impetus to the development of improvements and help to set the direction of such efforts.

Naturally, it is far better for the institution to avoid getting into vulnerable circumstances in the first place. The institution staff should take the initiative to meet necessary standards on its own, rather than simply reacting to the findings and recommendations of auditors. The best way to avoid adverse findings by auditors is to do an acceptable job before the audit takes place.

Expansion of the Auditors' Scope

A movement currently is underway by governmental auditors to insist on higher standards on the part of both auditees and themselves, and also to augment the numbers on their auditing staffs. This development will affect all institutional administration, not only financial administration.

The movement into performance auditing is receiving much attention and there appears to be some de-emphasis of financial audits. There are some reservations among business officers concerning the growing tendency of financial auditors to extend their activity beyond the area of financial administration into other phases of the operations of colleges and universities. There may be some doubt as to the competence of a financial auditor in doing a performance audit. Even a specialist on education may not be sufficiently qualified to warrant support when judging the performance of numerous experienced educators who have devoted their careers to their particular functions.

There is fear that such performance audits may have repercussions on the overall auditing effort and may undermine the professional prestige of auditors. If this development should be combined with a neglect of financial audits, the result would be damaging indeed to the acceptance of the auditing function.

Difficulty in Labeling Performance Audits

Some auditors also appear to be concerned about the acceptance of performance audits, as shown in their groping for a label that will be acceptable to auditees. Some suggest that the terms "management audit" and "performance audit" are too abrasive. "Program audit" may be too limiting. "Effectiveness audit" does not have the right ring. Some have settled on "operational audit," which may be a near-meaningless term in this context.

Where state auditors are concerned, it may be appropriate to devote resources to the upgrading of fiscal operations in the various states before extending efforts into unexplored areas.

A case can be made that more independent review and judgment of performance can be beneficial. The doubt lies in whether financial auditors are competent to conduct such activity. In higher education it would seem preferable to have teams of qualified, practicing educators appraise the performance of their counterparts. For example, the physics department of an institution can be evaluated by a competent team from the physics departments of other institutions. At least one institution is employing this device. In fact, periodic examinations by accrediting teams now constitute a type of performance audit in higher education.

In normal circumstances there are ways in which both the auditors and the staff of the institution can contribute toward improved mutual relationships in financial audits. The following points have been developed from experience and from discussion with financial officers of various corporations and institutions.

What the Institutional Staff Can Do

1. Endeavor to instill in its personnel an understanding of the role of auditors. Persons with financial responsibility should be encouraged to welcome an audit. Only with regular audits is there a degree of assurance to the individual that he or she and the department are adequately carrying out their responsibilities. Audits provide reassurance not only to the institutional staff but to the governing board, financial supporters, the federal government, the bondholders and, in the case of state institutions, the legislature and the citizens of the state.
2. Build effective communications with auditors. When a new situation arises, the institution can benefit by calling upon auditors to analyze its tentative position. If top-level administrators maintain a good relationship with auditors, the attitude will be reflected by subordinates.
3. Develop accounting and procedures manuals and keep them updated. Auditors may use the manuals as a source of reference, as a means of determining what internal controls are intended to be in effect in order to appraise them, and as an instrument to audit against.
4. Prepare annual financial statements and supporting work papers. Formats of both should be prepared in advance of year end. This makes the schedules part of the representation of the institution and increases the efficiency of the auditors.
5. Schedule work with the auditors and adhere to the schedules. Failure to have scheduled work ready will throw the entire program into chaos. The auditors are then over-staffed on the job. If they reassign staff to other auditees, the audit staff may not be available for the original job when the work is ready.

6. Encourage institutional personnel to be receptive to criticism and suggestions, to avoid a defensive attitude, and to consider recommendations honestly. Where no criticism is contained in the auditor's comments there is likely to be stagnation on both the part of the auditee-institution and on the part of the auditors. Almost invariably any change in internal control that helps or satisfies the auditors should already have been made for the benefit of the institution.
7. Take full responsibility for staff actions and inactions. It should consider itself to be accountable for the recommendations of the auditors. Each recommendation should be studied seriously. The institution's staff either should agree and implement the recommendation or it should disagree and give the reasons. To ignore recommendations is to manifest poor management.

What the Auditors Can Do

1. Continue the development toward appraisal of more than just the financial statements. *How* were the results brought about? Were the financial procedures haphazard or well-organized? Was the administrative process a burden or a help to the operation of institutional programs? As a result of their independence and their contacts with other operations, the auditors are qualified to make appraisals and suggestions regarding financial operations.
2. Consciously and continuously endeavor to be a model of good management. Auditors should plan the job, organize it by priorities, and then follow the plan. Perhaps auditors could make better use of internal controls over the performance of their own audits. More effort could be made to avoid overlapping of assignments and repetition of inquiries of the organization being audited. A good policy would be to complete each job in turn. When a number of jobs are only partially completed, there is wasted effort involved in the process of going back and finishing up.

   The overall audit should be considered incomplete until the report is released. Reportedly a performance audit of a midwestern university was released about four years following the field work. What is to be said about the performance of the auditors responsible for that performance audit? And of what value is it to the institution to receive an appraisal that is four years out of date? The auditors should adhere to the standards that they often expect of the institution in the clarity and coherency of their own work papers. There tends to be an undermining of confidence in the audit if the auditors refer to a deficiency and then are unable to identify it.
3. Work toward obtaining the respect and acceptance of the personnel of the organization being audited. Auditors should avoid cynicism and arrogance. When first entering a department, they should introduce themselves to the department head and explain their mission. They should be open and forthright in their work and try to develop an understanding of the work load of auditee personnel. They should not be disappointed when an auditee is already aware of a deficiency and is working to overcome it.
4. Give adequate recognition to practicality. Training as line managers would be valuable to auditors, since a manager constantly must make compromises between the ideal and the practical. Auditors should not over-emphasize a minor matter that would be costly to implement. They should remember that the college or university being audited must bear the financial responsibility for implementing any recommendation.
5. Know when to quit. Auditors need to identify the point at which the job should be concluded and then stop.
6. Retain their independence. An auditor is neither helping an institution by favoring it nor by criticizing unfairly. But the auditor who strives for fairness and objectivity will earn increasing respect.

While there is a natural tendency for individuals to be less than enthusiastic about any type of examination, the examination by auditors can be made to be less of an ordeal for all parties than it sometimes is. Both auditor and the auditee should consider that they have the same objectives and hence are not antagonists.

If the institutional house is in order, if the auditors are professional in stature and if both the staff of the auditee and the auditors take conscientious steps toward good relations, the result can be one of mutual benefit and satisfaction.

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